

Annual Report 1980

La Luz Mines Limited



La Luz

Board of Directors

Robert E. Fasken, Mississauga, Ontario
Mining Executive, Chairman, Camflo Mines Limited

K. G. R. Gwynne-Timothy, Q.C., Toronto, Ontario
Barrister and Solicitor

William J. McCormick, Oakville, Ontario
Executive

Brian K. Meikle, Mississauga, Ontario
Geologist, Vice President, Operations, Camflo Mines Limited

Robert M. Smith, Oakville, Ontario
Mining Engineer, President, Camflo Mines Limited

Officers (as at April 30, 1981)

Robert M. Smith — *President*

Robert E. Fasken — *Vice President*

Brian K. Meikle — *Vice President, Operations*

C. Bruce Burton — *Vice President, Finance*

William R. Robertson — *Secretary*

Kenneth E. Elrick — *Treasurer*

Transfer Agent and Registrar

Crown Trust Company
P.O. Box 38
1 First Canadian Place
Toronto, Canada

Auditors

Thorne Riddell
Toronto, Canada

Executive and Head Office

Suite 3001, South Tower, P.O. Box 45
Royal Bank Plaza
Toronto, Canada M5J 2J1

Annual Meeting of Shareholders

June 2, 1981, 11:00 a.m.
New Brunswick Room, Royal York Hotel
Toronto, Canada

Share Listing

The Toronto Stock Exchange
Share Symbol: LAZ

Bankers

The Royal Bank of Canada
Toronto, Canada

Directors' Report to the Shareholders

The Board of Directors submit herewith the Annual Report of the Corporation which includes the audited financial statements for the year ended December 31, 1980.

The main undertaking of the Corporation is operating two coal mines in Ohio. The Corporation also has minor oil and gas interests in Alberta, a small royalty interest in a tungsten mine in California and certain other investments.

In December 1980, the Corporation purchased all of the issued and outstanding shares of Gilbert Fuel Company which together with the Corporation's wholly-owned subsidiary La Luz Ohio, Inc., owns and operates the two open pit coal mines; Crown City and Muskingum, the former as a joint venture, the latter as a partnership.

FINANCIAL

The Corporation's share of coal revenue for the year ended December 31, 1980 was \$16,354,785 compared with \$12,406,921 for the same period in 1979. This increase resulted from an increase in both the tonnage sold and in the average price per ton received. (All dollars in this report are in U.S. currency.)

Other revenues during the twelve months ended December 31, 1980 include \$219,424 of petroleum and natural gas revenue compared with \$137,969 in 1979. Revenue from the Corporation's participation in a California tungsten mine declined significantly to \$5,000 in 1980 from \$55,485 in 1979.

At December 31, 1980, La Luz held 9,361 shares of Amax, Inc. and 100,000 shares of Camflo Mines Limited. These investments had a market value of \$3,906,000 at December 31, 1980. The Corporation has subsequently disposed of its investment in Amax.

The financial results of the two coal mines continue to be disappointing. The weak coal market and high rates of inflation and interest have prevented the realization of an economic return from these operations. During the year, improvements in

operations were achieved as demonstrated in the following table:

	1980	1979
Average price received per ton sold	\$28.90	\$24.90
Cost per ton before interest, royalty payment and depreciation	\$24.90	\$25.08

The extraordinarily high interest costs experienced throughout most of 1980 have significantly contributed to the Corporation's losses. Interest expense increased by over one million dollars to \$3,040,070 in 1980 from \$1,921,931 in 1979.

The consolidated net loss for the twelve months to December 31, 1980 was \$3,261,118 or \$2.06 per share after an extraordinary gain of \$1,104,584 compared with a net loss of \$4,183,313 or \$2.65 per share after an extraordinary gain of \$549,078 during the twelve month period ending December 31, 1979.

C.M.L. Inc., a subsidiary of Camflo Mines Limited, the parent of La Luz, continued to be a primary source of financing in 1980. Over \$6.7 million was provided during the year by C.M.L. Inc. As a result of similar funding of Gilbert Fuel Company, which La Luz acquired in late 1980, total indebtedness to C.M.L. Inc. increased to over \$18 million by year end.

OPERATIONS

Muskingum Mine

The Muskingum partnership owns approximately 17,000 surface acres overlaying leased coal of the #6 seam. Reserves, as determined by extensive drilling, are estimated to be in excess of 23 million tons, of which over 13 million tons are located between 10 to 80 feet of over-burden cover. Coal from this mine is sold, pursuant to a long-term contract expiring December 31, 1992, to the Conesville Generating Plant of A.E.P., which is located 8 miles from the mine. The contract calls for sales of 708,000 tons per year at a fixed price plus escalation for changes in the costs of producing, processing or transporting the coal.

In 1980, 680,000 tons were sold compared with 562,000 tons of coal for the year ended December 31, 1979. Sales were less than the contract requirements by 30,000 tons primarily due to the customer's equipment breakdown, a brief wildcat strike, and disruptions due to unfavourable weather conditions.

Efficiency at Muskingum gradually improved as the operators become more proficient with the larger stripping shovels. Later in the year some of the older bulldozers were replaced with a new D-10 and two Komatsu 4-55's. This will enable the mine to reduce the current reclamation backlog. Several old mine workings were encountered throughout the year resulting in disruptions in normal sequential mining. Planning is now being improved as more detailed engineering is implemented.

Crown City Mine

The Crown City joint venture owns approximately 10,000 surface acres including the coal and petroleum and natural gas rights. The property is located in Gallia and Lawrence Counties of Ohio. The property has been extensively drilled and reserves are estimated to be in excess of 11 million tons. Over 7 million tons lie under 10 to 60 foot over-burden cover lines. Coal from this mine is sold to American Electric Power under a 10 year cost escalation contract. The coal is treated at a company owned washing plant and then hauled 10 miles by independent truckers to the Ohio River, where it is loaded onto river barges owned by A.E.P.

In 1980, 452,000 washed tons were sold compared with 429,000 washed and raw tons of coal for the year ended December 31, 1979. Sales fell short of the contracted 500,000 tons of coal per year. Start-up problems associated with the mine's new coal washing facilities and a minor dispute over reclamation practices, which disrupted planned mining sequences, contributed to this

shortfall. These problems have been overcome and the entire mine and wash plant have become more efficient. The sales contract with the utility has been signed and regular price escalations are now being received. Consideration is also being given to the drilling this year of an exploratory gas well on the mine property.

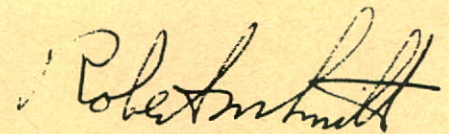
OUTLOOK

At Muskingum, a joint study is underway with A.E.P. to ascertain the optimum size and location of a wash plant and to determine whether some of the coal under greater depths of overburden should be mined.

Management is being reorganized and centralized at Columbus, Ohio. This will lead to improvements in accounting, purchasing and overall control of both operations.

More improvements in operations are necessary at both mines. Profitability will depend on increases which may be negotiated in the price of coal, the length of the current strike in the U.S. coal industry, the rate of inflation, new environmental regulations and interest rates. As the United States coal miners have been on strike for more than one month, the outlook for the coal operations in 1981 is not encouraging.

On behalf of the Board of Directors,



R. M. Smith,
President.

April 30, 1981.

La Luz Mines Limited

(Incorporated under the laws of Ontario)

Consolidated Balance Sheet

as at December 31, 1980

(Expressed in U.S. Dollars)

Assets	1980	1979
Current assets		
Cash	\$ 489,373	\$ 197,334
Accounts receivable	3,140,308	1,338,889
Mine operating supplies	1,448,988	751,400
Prepaid expenses	345,629	101,306
	<u>5,424,298</u>	<u>2,388,929</u>
Investments (note 2)	<u>1,342,464</u>	<u>1,664,297</u>
Fixed assets (note 3)	<u>31,955,614</u>	<u>15,206,806</u>
Other assets		
Preproduction expenditures, less amortization	2,173,418	1,149,719
Petroleum and natural gas interests, less depletion	325,729	365,748
Advance royalty payments (note 4)	669,855	303,818
Other	430,872	395,079
	<u>3,599,874</u>	<u>2,214,364</u>
	<u>\$ 42,322,250</u>	<u>\$ 21,474,396</u>
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities (note 5)	\$ 6,273,696	\$ 3,493,656
Advance payable to parent company	92,147	859,275
Current portion of long term liabilities	4,352,398	1,816,803
	<u>10,718,241</u>	<u>6,169,734</u>
Long term liabilities (note 6)	<u>33,637,727</u>	<u>14,077,262</u>
Capital stock and deficit		
Capital stock		
Authorized — 3,000,000 shares without par value		
Issued — 1,580,759 shares	3,372,829	3,372,829
Deficit	<u>5,406,547</u>	<u>2,145,429</u>
	<u>(2,033,718)</u>	<u>1,227,400</u>
	<u>\$ 42,322,250</u>	<u>\$ 21,474,396</u>

Contingent liabilities and commitments (note 7)

Approved by the Board


R. M. Smith, Director


B. K. Meikle, Director

Consolidated Statement of Operations

(Expressed in U.S. Dollars)

	Year ended December 31,		Six months ended
	1980	1979	December 31, 1979
Revenue			
Coal	\$ 16,354,785	\$ 12,406,921	\$ 6,811,352
Petroleum and natural gas	219,424	137,969	66,620
Royalties	5,000	55,485	6,135
	<u>16,579,209</u>	<u>12,600,375</u>	<u>6,884,107</u>
Operating and administrative expenses other than items set out below	15,880,653	13,688,032	6,795,946
Interest on long term liabilities	3,040,070	1,921,931	1,112,869
Depreciation, depletion and amortization	2,193,091	1,761,969	877,166
	<u>21,113,814</u>	<u>17,371,932</u>	<u>8,785,981</u>
Loss before the undernoted	(4,534,605)	(4,771,557)	(1,901,874)
Investment and other income	168,903	87,633	72,525
Loss before income taxes and extraordinary item	(4,365,702)	(4,683,924)	(1,829,349)
Income taxes		48,467	
Loss before extraordinary item	(4,365,702)	(4,732,391)	(1,829,349)
Gain on sale of investment	1,104,584	549,078	55,164
Loss for the period	<u>\$ (3,261,118)</u>	<u>\$ (4,183,313)</u>	<u>\$ (1,774,185)</u>
Loss per share			
Loss before extraordinary item	\$ (2.76)	\$ (2.99)	\$ (1.16)
Loss for the period	\$ (2.06)	\$ (2.65)	\$ (1.12)

Consolidated Statement of Deficit

(Expressed in U.S. Dollars)

	Year ended December 31,		Six months ended
	1980	1979	December 31, 1979
Retained earnings (deficit) at beginning of period	\$ (2,145,429)	\$ 2,037,884	\$ (371,244)
Loss for the period	<u>3,261,118</u>	<u>4,183,313</u>	<u>1,774,185</u>
Deficit at end of period	<u>\$ 5,406,547</u>	<u>\$ 2,145,429</u>	<u>\$ 2,145,429</u>

Consolidated Statement of Changes in Financial Position

(Expressed in U.S. Dollars)

	Year ended December 31,		Six months ended December 31,
	1980	1979	1979
Working capital derived from			
Proceeds on sale of			
Investment in other company	\$ 1,426,417	\$ 1,397,585	\$ 132,164
Fixed assets	43,810	3,164	
Petroleum and natural gas interests		31,378	
Advances from affiliated company	6,717,583	2,769,841	1,606,314
Increase in long term liabilities	4,210,059	3,340,665	1,853,362
	<u>12,397,869</u>	<u>7,542,633</u>	<u>3,591,840</u>
Working capital applied to			
Operations	2,172,611	2,970,149	959,829
Additions to fixed assets	1,874,292	4,425,371	2,649,357
Retirement of long term liabilities	3,593,185	1,277,474	940,742
Acquisition of subsidiary (note 10)	3,300,000		
Working capital deficiency assumed on acquisition of subsidiary (note 10)	2,797,238		
Other assets, net	173,681	692,612	369,030
	<u>13,911,007</u>	<u>9,365,606</u>	<u>4,918,958</u>
Decrease in working capital position	1,513,138	1,822,973	1,327,118
Working capital deficiency at beginning of period	3,780,805	1,957,832	2,453,687
Working capital deficiency at end of period	\$ 5,293,943	\$ 3,780,805	\$3,780,805

AUDITORS' REPORT

To the Shareholders of
La Luz Mines Limited

We have examined the consolidated balance sheet of La Luz Mines Limited as at December 31, 1980 and December 31, 1979 and the consolidated statements of operations, deficit and changes in financial position for the years then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1980 and 1979 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles applied on a consistent basis.

Toronto, Canada
March 27, 1981

Thorne Riddell
Chartered Accountants

Notes to Consolidated Financial Statements

YEAR ENDED DECEMBER 31, 1980
(Expressed in U.S. Dollars)

The company is incorporated in the Province of Ontario under The Business Corporations Act and is a public company listed on The Toronto Stock Exchange. As at December 31, 1980 approximately 58% of the issued shares of the company were owned by Camflo Mines Limited. The principal activities of the company consist of coal mining operations in the State of Ohio, U.S.A. through its wholly owned subsidiary La Luz Ohio, Inc. operating under the names of Crown City Mining Company and Muskingum Mining Company (referred to collectively herein as the coal enterprises).

1. Summary of Significant Accounting Policies

- (a) Basis of consolidation
These consolidated financial statements include the accounts of the company and its wholly owned U.S. subsidiaries, Panaminas Incorporated and La Luz Ohio, Inc. (See note 10). All material intercompany transactions have been eliminated.
- (b) Mine operating supplies
Mine operating supplies are recorded at cost.
- (c) Depreciation, depletion and amortization
 - (i) Coal
The company uses the unit of production method to compute depletion on coal lands and depreciation and amortization on the major portion of the property, buildings and equipment and preproduction expenditures.
 - (ii) Petroleum and natural gas
The company follows the full cost method of accounting for its petroleum and natural gas interests whereby all costs related to the exploration for and development of petroleum and natural gas reserves are capitalized. Such costs include land acquisition costs, geological and geophysical expenses, carrying charges on non-producing property, costs of drilling both productive and unproductive wells and related production equipment. Proceeds received on disposal of properties are ordinarily credited against such costs. Depreciation and depletion are provided on the net costs using the composite unit of production method based on total estimated proven reserves.
- (d) Basis of translation of Canadian currency
Canadian currency has been translated as follows:
 - (i) Current assets and liabilities, at exchange rates prevailing at the period end.
 - (ii) All other assets and liabilities, at exchange rates prevailing at the date the assets were acquired or the liabilities incurred.
 - (iii) Revenues and expenses, at the average exchange rate for the period except for depreciation, depletion and amortization which are based on the cost of assets as translated.

(iv) Unrealized foreign exchange gains and losses are included in operations.

- (e) Reclamation costs
Reclamation costs are accrued in the accounts based on the anticipated costs of completing the restoration of acreage affected by mining operations as determined by management.
- (f) Change of year end
During 1979 the company changed its fiscal year end from June 30 to December 31.

2. Investments

	1980	1979
Shares, at cost (quoted market value \$3,906,000; 1979, \$3,101,000) Amax, Inc. (formerly Rosario Resources Corporation)	\$ 104,660	\$ 426,493
Camflo Mines Limited	1,237,804	1,237,804
	<u>\$ 1,342,464</u>	<u>\$ 1,664,297</u>

3. Fixed Assets

	1980	1979
Land	\$ 8,915,441	\$ 3,586,266
Buildings	1,606,737	809,354
Machinery and equipment	28,450,334	13,800,224
Washing and preparation plant	2,417,487	1,149,060
Equipment under capital leases	384,035	330,939
Vehicles	951,610	423,477
Furniture and fixtures	66,979	24,773
	<u>42,792,623</u>	<u>20,124,093</u>
Less accumulated depreciation and depletion	10,837,009	4,917,287
	<u>\$31,955,614</u>	<u>\$15,206,806</u>

4. Advance Royalty Payments

Certain coal mining rights have been leased in consideration for a royalty payment of \$3.51 per ton on the greater of 700,000 tons per year or the coal produced and shipped in the year. The lease is for a term of twenty years ending October 31, 1998 subject to the lessee's right to surrender the lease at any earlier time when all economically mineable coal has been mined or minimum royalties on 14,000,000 tons have been paid. The lease may be renewed for successive three year periods. Royalties paid in excess of coal produced and shipped in the year can be applied against royalties due in a subsequent lease year on production in excess of the annual minimum tonnage requirements.

5. Accounts Payable and Accrued Liabilities

	1980	1979
Trade and other	\$ 3,553,678	\$ 2,014,308
Related companies	56,145	118,004
Accrued reclamation costs	2,663,873	1,361,344
	<u>\$ 6,273,696</u>	<u>\$ 3,493,656</u>

6. Long Term Liabilities

	1980	1979
Notes payable	\$12,584,782	\$ 5,025,530
Short term obligations expected to be refinanced		96,230
Mortgage payable	6,682,000	4,129,000
Capital leases	347,426	235,590
Loans and notes payable, affiliated company	18,375,917	6,407,715
	37,990,125	15,894,065
Less instalments due within one year	4,352,398	1,816,803
	<u>\$33,637,727</u>	<u>\$14,077,262</u>

Instalments due in each of the next five years are approximately as follows:

1981	\$4,352,000
1982	5,538,000
1983	3,891,000
1984	3,633,000
1985	1,478,000

Notes payable	1980	1979
Notes payable, secured by certain equipment of the coal enterprises, bearing interest at rates varying from 7% to U.S. prime rate plus 2½% maturing approximately as follows:		
1981, \$2,216,000;		
1982, \$2,210,000;		
1983, \$1,868,000;		
1984, \$1,269,000;		
1985, \$ 625,000;		
1986, \$1,128,000	\$ 9,316,032	\$ 4,046,217

Notes payable, secured by the coal washing plant and the same collateral securing the mortgage payable (see below) bearing interest at U.S. prime plus 2% and repayable in 24 quarterly instalments of \$93,750 commencing May 1, 1980	1,968,750	979,313
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Notes payable, unsecured, bearing interest at 6% maturing January 15, 1982	1,300,000	
	<u>\$12,584,782</u>	<u>\$ 5,025,530</u>

Mortgage Payable

The mortgage payable bears interest at 2% above the lender's New York prime commercial rate payable monthly. Principal repayments of \$394,000 are to be made quarterly until January 1, 1985 at which time the entire unpaid balance becomes due. Principal repayments may be accelerated under certain conditions. The mortgage is secured by the company's investment in the coal enterprises including liens upon substantially all of their assets and a pledge of marketable securities. The company's parent has also guaranteed repayment of a portion of the loan.

In addition to the aforementioned payments, within 90 days after June 30, the coal enterprises must also make additional annual payments on principal in the amount of 80% of their cash flow as calculated in the loan agreement. Such additional payments shall be applied to principal in inverse order of maturity. As of December 31, 1980, no additional payments have been required.

Capital leases

Capital leases represent the present value of the net minimum lease payments, as at December 31, 1980, calculated at the lessor's implicit interest rates, which vary from 8½% to 11%. The leases are secured by a pledge of certain machinery and equipment.

Loans and notes payable, affiliated company

	1980	1979
Loans payable, secured by certain of the company's assets bearing interest at U.S. prime interest rate plus 1½% (1979, 125% of the U.S. prime interest rate) maturing January 31, 1986	\$17,875,917	\$ 6,207,715
Notes payable, unsecured, bearing interest at 18%, maturing October 9, 1984, \$400,000; January 29, 1985, \$100,000	500,000	200,000
	<u>\$18,375,917</u>	<u>\$ 6,407,715</u>

7. Contingent Liabilities and Commitments

- In consideration of the guarantee of the mortgage payable (note 6) and certain reclamation bonds (note 7(b)), the coal enterprises have agreed to pay a commitment fee to the parent company of \$.30 per ton on all coal mined and sold.
- As of December 31, 1980 the company has furnished surety bonds in the approximate amount of \$13,227,000 to the State of Ohio to ensure the restoration of land affected by strip mining.

- (c) Under the terms of the lease covering certain coal mining rights (note 4), the Muskingum Mining Company is required to maintain \$2,000,000 working capital as defined. As at December 31, 1980, and subsequent thereto, Muskingum was not in compliance with this covenant. The lessor has waived this default to December 31, 1981 in consideration of the parent company undertaking to provide sufficient funds to maintain operations to that date.

8. Related Party Transactions

- (a) Operating and administrative expenses include \$1,333,000 (twelve months 1979, \$823,000; six months 1979, \$429,000) allocated by related companies in connection with sharing certain office premises and administrative services and commitment fees and \$13,800 (twelve months 1979, \$900; six months 1979, \$900) paid to a legal advisor who is also a director of the company. Interest expense includes \$1,513,000 (twelve months 1979, \$868,000; six months 1979, \$540,000) charged by related companies. Investment and other income includes \$85,600 (twelve months 1979 \$60,000, six months 1979 \$34,000) from a related company.
- (b) All of the company's coal revenues are derived from sales to electric power utilities located in the State of Ohio.

9. Income Taxes

The company and its subsidiaries have non-capital losses and other tax credits of approximately \$17,472,000 for which tax benefits were not recorded in the accounts. These losses and tax credits are available for carry forward to future years and are restricted to fiscal years not later than:

1981	\$2,384,000
1982	2,450,000
1983	2,223,000
1984	14,000
1985	185,000
1986	3,169,000
1987	7,047,000

10. Acquisition of Subsidiary

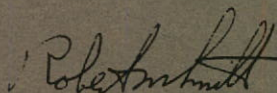
Effective December 30, 1980 the company's subsidiary, La Luz Ohio, Inc., acquired 100% of the issued shares of Gilbert Fuel Co., the other 50% partner and joint venturer in the coal enterprises. Gilbert's results of operations for the year are not included in the consolidated statement of operations. Details of the acquisition, which has been accounted for by the purchase method, are as follows:

Net assets acquired at fair values assigned thereto

Fixed assets	\$16,739,312
Other assets	1,583,933
	<u>18,323,245</u>
Working capital deficiency	2,797,238
Long term liabilities	12,226,007
	<u>15,023,245</u>
	<u>\$ 3,300,000</u>
Consideration	
Cash	\$ 2,000,000
6% Notes payable due	
January 15, 1982	1,300,000
	<u>\$ 3,300,000</u>

MANAGEMENT REPORT

The annual report and financial statements have been prepared by management and approved by the Board of Directors. The financial statements have been prepared in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year. Management acknowledges responsibility for the fairness, integrity and objectivity of all financial information contained in the annual report including the financial statements.


R. M. Smith, President


C. B. Burton, V.P. Finance

